

# McDowell & Rackner PC



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November 25, 2008

## VIA ELECTRONIC FILING AND FIRST CLASS MAIL

PUC Filing Center  
Public Utility Commission of Oregon  
PO Box 2148  
Salem, OR 97308-2148

**Re: Docket UM \_\_\_\_\_ – Stipulation and Parties' Brief in Support of Stipulation**

Enclosed for filing are the original and five copies of the Stipulation and the Parties' Brief in Support of Stipulation for PUC Staff, Citizens' Utilities' Board of Oregon, Northwest Industrial Gas Users, and Northwest Natural Gas submitted by Lisa Rackner.

A copy of this filing has been served on the parties indicated on the attached certificate of service.

Very truly yours,

A handwritten signature in black ink, appearing to read "Amie Jamieson".

Amie Jamieson

Enclosure

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**CERTIFICATE OF SERVICE**

I hereby certify that I served a true and correct copy of the foregoing document in this proceeding on the following named person(s) on the date indicated below by email and/or first-class mail addressed to said person(s) at his or her last-known address(es) indicated below.

Chad Stokes  
Cable Huston Benedict  
Haagensen & Lloyd  
cstokes@cablehuston.com

Jason Jones  
Department of Justice  
Regulated Utility & Business Section  
1162 Court St NE  
Salem, OR 97301-4096  
jason.w.jones@state.or.us


Paula E Pyron  
Executive Director  
Northwest Industrial Gas Users  
ppyron@nwigu.org

Carla Owings  
PO Box 2148  
Salem, OR 97308-2148  
carla.m.owings@state.or.us

Bob Jenks  
bob@oregoncub.org  
  
dockets@oregoncub.org

G. Catriona McCracken  
catriona@oregoncub.org

DATED: November 25, 2008.

  
\_\_\_\_\_  
Amie Jamieson

McDowell & Rackner PC

**BEFORE THE PUBLIC UTILITY COMMISSION  
OF OREGON**

UM \_\_\_\_\_

In the Matter of  
NORTHWEST NATURAL'S System Integrity  
Program

**STIPULATION**

This Stipulation is entered into for the purposes of renewing existing programs for Bare Steel and Transmission Integrity Management; consolidating such programs into a single System Integrity Program ("SIP"); and including within the SIP a new program for Distribution Integrity Management. The new integrated SIP, with its three focus areas, will allow for a risk-based approach to addressing system integrity issues.

**PARTIES**

1. The Parties to this Stipulation are Northwest Natural Gas Company ("NW Natural"), the Public Utility Commission of Oregon Staff, the Citizens' Utility Board of Oregon, and the Northwest Industrial Gas Users (collectively, the "Parties").

**BACKGROUND**

2. NW Natural has maintained a number of safety programs. These included a Cast Iron Replacement Program and a Geohazard Program, both of which have been discontinued.<sup>1</sup> They now include the Transmission Integrity Management Program ("TIMP"), which was initiated in 2002 in response to the Pipeline Safety Improvement Act of 2002 ("2002

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<sup>1</sup> Some of the activities that had previously been conducted under the Geohazard program will now be properly conducted under the TIMP and/or DIMP programs, as required by applicable federal regulations.

Improvement Act”) and PHMSA<sup>2</sup> Natural Gas Integrity Management Rule, and the Bare Steel Replacement Program (“Bare Steel Program”), which was approved by the Commission in 2001 and had an original completion date of 2021.

3. The Pipeline Inspection, Protection, Enforcement and Safety Act of 2006 (“2006 PIPES Act”) expands requirements of the 2002 Improvement Act by requiring PHMSA to prescribe minimum standards for Distribution Integrity Management Programs (“DIMPs”) to cover the integrity and broader aspects of distribution mains, services, and other gas related appurtenances. In addition, the 2006 PIPES Act significantly expands the requirements of all stakeholders relative to excavation damage prevention.

4. While previously implemented separately, the NW Natural’s Cast Iron, Bare Steel, and Geohazard programs all were designed to address the issues raised and regulations formulated as a result of federal legislation to improve natural gas transmission and distribution system safety. Going forward, it would be difficult to separate these critical programs from regulations that have emerged, and will emerge in the future, from the 2002 and 2006 safety acts. Each individual program plays an integral part in ensuring that the NW Natural complies with the legislative and regulatory framework. It is also evident based upon past history that variations in work load in each category will invariably occur.

5. NW Natural is requesting renewal and consolidation of existing programs for Bare Steel and TIMP, and inclusion of DIMP, into a single System Integrity Program. The new, integrated program with its three focus areas will allow for a risk-based approach to addressing system integrity issues.

#### **AGREEMENT**

6. **Accounting Treatment.** The Parties agree to support NW Natural’s request for an accounting order to classify SIP costs as capital costs.

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<sup>2</sup> U.S. Department of Transportation Pipeline and Hazardous Materials Safety Administration.

7. **Cost Tracking.** NW Natural will track SIP costs on a project basis. Project costs would accumulate in capital accounts that would be designated as SIP activities and would be traced by NW Natural on a per job basis. NW Natural would track the SIP investment annually to obtain a total account for each year, with the proposed tracking period running from November 1 to October 31 ("Tracker Year").<sup>3</sup>

8. **Cost Recovery.** NW Natural will not seek recovery through the proposed annual rate adjustment for: 1) current O&M funding embedded in rates of approximately \$574 thousand per year; 2) additional O&M costs related to DIMP damage prevention; 3) the first \$3 million in combined bare steel and leakage capital costs, and 4) an additional \$250,000 in SIP capital costs.

On an annual basis, the most recent actual SIP costs incurred during the period from November 1 prior to the PGA filing date plus an estimate of activity through October 31 would be used to determine the SIP Cost of Service (as described in Paragraph 9) for the relevant year. The SIP Cost of Service would be included in the NW Natural's PGA subject to an audit by OPUC Staff. Upon Commission approval of the SIP Cost of Service, an adjustment would be made to permanent rates (Schedules 1-3, 31, 32, 33 and 54) effective October 1 during the term of the revenue recovery period, in accordance with the allocation methods described in paragraph 11 below.

9. **Cost of Service.** The SIP Cost of Service would be identified using the same process that was used in the previous UM 1156/TIMP costs and UM 1030/Bare Steel and Geohazard Risk Mitigation Costs. See Order Nos. 04-390, 02-687, 01-843, Schedule 177 and the Stipulation entered into August 3, 2001 between NW Natural and Staff. That is, for each recovery period, NW Natural would develop a cost of service for the SIP investment which would include incremental depreciation, expense, property tax, return, income taxes and other costs customarily relating to utility investment. The capital structure and the cost of long term

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<sup>3</sup> For the 2008-2009 year, the relevant period would be October 1, 2008 through October 31, 2009.

debt and preferred stock to be used in the calculation of a return on rate base would be those adopted by the Commission in NW Natural's most recent rate case.

The Parties agree that, subject to audit, rates would be adjusted each fall within NW Natural's PGA, in the same manner used for recovery of costs under the previous integrity management program, as approved in Order No. 04-390.

10. **Recovery Cap.** Total annual SIP expenditures would have a soft cap of \$12 million per Tracker Year (\$8.176 million recoverable through cost of service), excluding 2008 where current program approvals for Bare Steel and Transmission Integrity are applicable. Program expenditures could only exceed \$12 million in a Tracker Year with the written consent of OPUC Staff, NWIGU, and CUB.

11. **Program Parts.** The Parties agree that costs would be recovered through one adjustment schedule comprised of parts for each program. Attached as Exhibit A is Draft Revised Schedule 177, reflecting these changes.

a. Part A will account for costs related to the Bare Steel Replacement Program. NW Natural will allocate seventy percent (70%) of the cumulative investment to Residential and Commercial firm sales and transportation customers taking service under Rate Schedules 1, 2, 3, 31, and 54 on an equal cents per therm basis. The remaining 30% will be allocated on an equal percent of margin basis to all customer classes and within a rate schedule shall be spread on a declining block basis. The cost recovery for this part shall be as agreed to in Order No. 04-390.

b. Part B will account for costs related to TIMP. Part B costs will be spread to all customer classes on an equal percent of margin and within a rate schedule shall be spread on a declining block basis.

c. Part C will account for costs related to DIMP. Part C costs will be spread to all customer classes on an equal percent of margin and within a rate schedule shall be spread on a declining block basis.

12. **Annual Forecast.** Each April, OPUC Staff, NWIGU, and CUB will receive a forecast of expenses through October 31, 2011, broken down into Parts A, B, and C, as described above; however, NW Natural will have the flexibility to shift dollars between the three Parts based on NW Natural's assessment of annual risk and need.

13. **Annual Report.** Each August, NW Natural will provide OPUC Staff, NWIGU, and CUB a report of actual expenses by Tracker Year broken down by specific projects and initiatives.

14. **Bare Steel.** In 2001, the OPUC Staff and NW Natural entered into a Bare Steel Stipulation to allow NW Natural to replace its bare steel distribution and transmission facilities within twenty years. See attached Exhibit B. The intent of the SIP Stipulation is to allow, for the term of the SIP Stipulation, funds previously earmarked for bare steel to be shifted among all three of the SIP Parts (Parts A, B, and C). To that extent, the SIP Stipulation overrides any inconsistent provisions in the Bare Steel Stipulation.

NW Natural will maintain its obligation under the Bare Steel Stipulation to complete the replacement of its bare steel distribution and transmission facilities by 2021. Upon expiration of the SIP Stipulation, the Parties agree that the Bare Steel Stipulation will remain in effect.

15. **Commission May Request Rate Case.** After July 1, 2009, if NW Natural is not already engaged in a general rate filing, the Commission may request that NW Natural submit a general rate filing in Oregon no later than eight months thereafter. NW Natural shall bear the burden of proof in such filing, in accordance with ORS 757.210.

Because this provision could be viewed as inconsistent with the WARM/decoupling stipulation, we have consulted with the other parties to that Stipulation on this provision. NW Energy Coalition, CAPO and DOE have confirmed that they have no objection. To the extent necessary, this provision will overrule any inconsistent provisions of the WARM/decoupling stipulation.

16. **Term.** This Stipulation shall apply to costs incurred after September 30, 2008, and shall apply to costs incurred the earlier of October 31, 2011, or until the effective date of new rates adopted in the Company's next general rate case.

17. **Integrated Document.** The Parties have negotiated this Stipulation as an integrated document. If the Commission rejects all or any material portion of this Stipulation or imposes additional material conditions in approving this Stipulation, any party disadvantaged by such action shall have the rights provided in OAR 860-014-0085 and shall be entitled to seek reconsideration or appeal of the Commission's Order.

18. By entering into this Stipulation, no party shall be deemed to have approved, admitted, or consented to the facts, principles, methods, or theories employed by any other party in arriving at the terms of this Stipulation. No party shall be deemed to have agreed that any provision of this Stipulation is appropriate for resolving issues in any other proceeding.

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19. This Stipulation may be executed in counterparts and each signed counterpart shall constitute an original document.

This Stipulation is entered into by each party on the date entered below such party's signature.

NORTHWEST NATURAL GAS COMPANY

CITIZENS' UTILITY BOARD OF OREGON

By C. Alex Miller  
C. Alex Miller  
Director, Regulatory Affairs and  
Forecasting

By \_\_\_\_\_  
Robert Jenks  
Executive Director

Date: 11/25/08

Date: \_\_\_\_\_

NORTHWEST INDUSTRIAL GAS USERS

STAFF OF THE PUBLIC UTILITY  
COMMISSION OF OREGON

By: \_\_\_\_\_  
Paula E. Pyron  
Executive Director

By: \_\_\_\_\_  
Jason Jones  
Attorney for Staff  
Oregon Department of Justice

Date: \_\_\_\_\_

Date: \_\_\_\_\_

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CITIZENS' UTILITY BOARD OF OREGON

By \_\_\_\_\_  
C. Alex Miller  
Director, Regulatory Affairs and  
Forecasting

By \_\_\_\_\_  
Robert Jenks  
Executive Director


Date: \_\_\_\_\_

Date: \_\_\_\_\_

NORTHWEST INDUSTRIAL GAS USERS

STAFF OF THE PUBLIC UTILITY  
COMMISSION OF OREGON

By \_\_\_\_\_  
Paula E. Pyron  
Executive Director

By  \_\_\_\_\_  
Jason Jones  
Attorney for Staff  
Oregon Department of Justice

Date: \_\_\_\_\_

Date: 11/25/08

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By \_\_\_\_\_  
C. Alex Miller  
Director, Regulatory Affairs and  
Forecasting

By \_\_\_\_\_  
Robert Jenks  
Executive Director

Date: \_\_\_\_\_

Date: \_\_\_\_\_

NORTHWEST INDUSTRIAL GAS USERS

STAFF OF THE PUBLIC UTILITY  
COMMISSION OF OREGON

By: Paula E. Pyron  
Paula E. Pyron  
Executive Director

By: \_\_\_\_\_  
Jason Jones  
Attorney for Staff  
Oregon Department of Justice

Date: 11/24/2008

Date: \_\_\_\_\_

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NORTHWEST NATURAL GAS COMPANY

CITIZENS' UTILITY BOARD OF OREGON

By \_\_\_\_\_  
C. Alex Miller  
Director, Regulatory Affairs and  
Forecasting

By   
Robert Jenks  
Executive Director

Date: \_\_\_\_\_

Date: 11/25/08

NORTHWEST INDUSTRIAL GAS USERS

STAFF OF THE PUBLIC UTILITY  
COMMISSION OF OREGON

By: \_\_\_\_\_  
Paula E. Pyron  
Executive Director

By: \_\_\_\_\_  
Jason Jones  
Attorney for Staff  
Oregon Department of Justice

Date: \_\_\_\_\_

Date: \_\_\_\_\_

**Exhibit A**  
to System Integrity Program Stipulation  
Dated November 25, 2008

Draft Revised Schedule 177

# NORTHWEST NATURAL GAS COMPANY

P.U.C. Or. 24

Second Revision of Sheet 177-1  
Cancels First Revision of Sheet 177-1

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## SCHEDULE 177 SYSTEM INTEGRITY PROGRAM RATE ADJUSTMENT

### **PURPOSE:**

To recover the costs associated with the Company's System Integrity Program according to Commission Order 08-XXX and the stipulated terms and conditions included as Appendix A to this Order.

### **GENERAL TERMS:**

This Schedule is governed by the terms of this Schedule, the General Rules and Regulations contained in this Tariff and by all rules and regulations prescribed by regulatory authorities, as amended from time to time.

### **SYSTEM INTEGRITY PROGRAM ADJUSTMENT RATE**

The System Integrity Program Adjustment Rate recovers the costs incurred from the Company's System Integrity Program which consists of the following parts:

**Part A – Bare Steel Replacement Program** This program was initiated in 2001 with an estimated completion date of schedule of 2021. The costs for this program will be classified as capital expenditures. The Company will allocate 70% of the cumulative investment to Residential and Commercial firm sales and transportation customers taking service under Rate Schedules 1, 2, 3, 31 and 54 on an equal cents per therm basis. The remaining 30% will be allocated on an equal percent of margin basis to all customer classes. The cost recovery for this Part shall be as agreed to in the Safety Program Stipulation, dated April 17, 2002.

**Part B –Transmission Integrity Management Program (TIMP)** – This program was initiated in 2002 in response to the Pipeline Safety Improvement Act of 2002 and PHMSA Natural Gas Integrity Management Rule. Associated costs will be spread to all customer classes on an equal percent of margin.

**Part C - Distribution Integrity Management Program (DIMP)** – This program was initiated in 2008 and will focus on damage prevention. Associated costs will be spread to all customer classes on an equal percent of margin.

### **SPECIAL PROVISIONS**

1. The per annum cost recovery under this adjustment rate schedule shall not exceed \$12 million dollars without express written consent from all parties to the Stipulation attached to Commission Order 08-XXX as Appendix A.
2. In April, the Company will provide parties to UG-XX an annual forecast of program expenditures and in August, a report of actual program spending compared with annual collections under this adjustment schedule.

(continue to Sheet 177-2)

Issued Month X, 2008  
NWN Advice No. OPUC 08-XX

Effective with service on  
and after Month X, 2008

# NORTHWEST NATURAL GAS COMPANY

P.U.C. Or. 24

Third Revision of Sheet 177-2  
Cancels Second Revision of Sheet 177-2

## SCHEDULE 177 SYSTEM INTEGRITY PROGRAM RATE ADJUSTMENT

### SPECIAL PROVISIONS (Continued)

3. The rate adjustment will be changed each October with a November 1 effective date. The rate change will be based on actual and forecasted expense and investment activity through September 30 and adjusted to reflect the difference between the previous year's actual versus forecasted costs.

### **TERM:**

This adjustment rate shall be in effect through December 31, 2021 or until such other time as the Commission may approve.

### **APPLICATION TO RATE SCHEDULES:**

**Effective: November 1, 2008**

The Adjustments shown below are included in the Base Adjustments in the listed Rate Schedules:

Schedule	Block	Part A		Part B	Part C	Total Adjustment
		70%	30%			
1R		\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
1C		\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
2		\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
3 (CSF)		\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
3 (ISF)		\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
19		\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
31 (CSF)	Block 1	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
	Block 2	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
31(CTF)	Block 1	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
	Block 2	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
31 (CSI)	Block 1	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
	Block 2	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
31 (ISF)	Block 1	n/a	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
	Block 2	n/a	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
31 (IFT)	Block 1	n/a	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
	Block 2	n/a	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
31 (ISI)	Block 1	n/a	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
	Block 2	n/a	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
32 (all)	Block 1	n/a	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
	Block 2	n/a	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
	Block 3	n/a	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
	Block 4	n/a	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
33 (all)	Block 5	n/a	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
	Block 6	n/a	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
		n/a	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX
54		\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX	\$0.XXX

Issued Month X, 2008  
NWN Advice No. OPUC 08-XX

Effective with service on  
and after Month X, 2008

**Exhibit B**  
to System Integrity Program Stipulation  
Dated November 25, 2008

2001 Bare Steel Stipulation in Docket UM 1030



RECEIVED

OCT - 2 2001

RATES &  
REGULATORY AFFAIRS

ORDER NO 01-843'

ENTERED SEP 28 2001

**BEFORE THE PUBLIC UTILITY COMMISSION**

**OF OREGON**

UM 1030

In the Matter of the Application of )  
NORTHWEST NATURAL for Deferred ) ORDER  
Accounting of Safety Program Costs. )

**DISPOSITION: DEFERRED ACCOUNTING APPLICATION APPROVED**

On August 29, 2001, Northwest Natural (NW Natural) filed an application with the Public Utility Commission of Oregon (Commission), pursuant to ORS 757.259, for an accounting order requesting authorization to defer safety program costs. A description of the filing and its procedural history is contained in the Staff Report and supporting exhibits, attached as Appendix A, and incorporated by reference.

At its Public Meeting on September 25, 2001, the Commission adopted Staff's Recommendations 1, 2, and 3. Only Recommendation 3, the application for an accounting order, requires a Commission order.

**ORDER**

IT IS ORDERED THAT Northwest Natural's application for an accounting order regarding authorization of deferred accounting for safety program costs, as described in Appendix A, is granted. This approval is for accounting purposes only.

Made, entered and effective SEP 28 2001



BY THE COMMISSION:

*Vikie Bailey Goggins*  
Vikie Bailey Goggins  
Commission Secretary

A party may request rehearing or reconsideration of this order pursuant to ORS 756.561. A party may appeal this order to a court pursuant to ORS 756.580.

**FILE**

PUBLIC UTILITY COMMISSION OF OREGON  
 STAFF REPORT  
 PUBLIC MEETING DATE: September 25, 2001

REGULAR  CONSENT  EFFECTIVE DATE October 1, 2001

DATE: September 19, 2001

TO: Phil Nyegaard through Lee Sparling <sup>us</sup>

FROM: Bonnie Tatom <sup>bbt</sup>

SUBJECT: NW Natural Advice No. OPUC 01-20

**SUMMARY RECOMMENDATION:**

I recommend the Commission: (1) allow the tariff sheets filed in Advice No. 01-20 to go into effect on October 1, 2001, (2) approve the rate spread used to spread the costs of the Bare Steel Replacement Program, (3) approve the company's deferred accounting application for its safety program costs (the Bare Steel Replacement and the Geohazard Risk Mitigation and Repair programs), and (4) approve the Stipulation, dated August 3, 2001, between NW Natural and Staff regarding rate treatment for NW Natural Safety Programs. This filing does not change the company's annual revenues at this time.

**DISCUSSION:**

On August 29, 2001, NW Natural submitted Schedule 177, "Revision of Charges for Bare Steel Replacement Program." The purpose of the filing is to include in the company's tariff, a schedule designed to recover costs associated with the company's accelerated bare steel replacement program. The company also included an application for deferred accounting of its safety program costs.

History

Over the last year, NW Natural, Staff, Citizens' Utility Board (CUB), and Northwest Industrial Gas Users (NWIGU) met to discuss the appropriate treatment of costs associated with the company's safety programs. These programs include the accelerated replacement of the company's bare steel distribution and transmission facilities and geohazard risk mitigation. The two significant issues concerning NW Natural's safety programs were (1) whether the company should accelerate bare steel replacement and how customers should pay for the company's investment and costs associated with the accelerated program, and (2) whether the company should pursue geohazard risk

NW Natural Advice No. OPUC 01-20 Bare Steel Replacement Program  
September 19, 2001  
Page 2

mitigation and how customers should pay for those activities. Following is a brief synopsis of these two issues:

#### Bare Steel Replacement

Early this year, Staff met with NW Natural to discuss its safety programs. PUC Safety & Reliability staff have been concerned for some time that the company's normal time frame for replacing corrosion-subject bare steel would likely result in higher costs of detecting and repairing leaks, and more importantly, impair the company's excellent service quality and safe distribution system. The bare steel has been in the ground for many years—some since the 1940s. With its current schedule, the company would not have completely replaced its bare steel system until roughly 2038. The company proposed a Stipulation that would allow the company to cut nearly in half the time frame necessary to replace the bare steel to the end of 2021. NW Natural is currently investing about \$3 million annually in bare steel replacement activities. The Stipulation allows the company to invest as much as \$6 million in its bare steel replacement activities, with the incremental \$3 million considered as accelerated bare steel replacement costs. The Stipulation further defines how these costs may be included in rates. At the time of the annual Purchased Gas Adjustment (PGA) filing, or some other suitable filing, NW Natural may include in rates, the cost of service associated with the entire accelerated bare steel replacement for the most recent 12-month period. Exhibit A to the Stipulation shows how the company will develop a cost of service for each year's accelerated bare steel replacement program costs.

#### Geohazard Risk Mitigation and Repair

Another concern to PUC Safety Staff is the health and safety risk associated with geohazards, defined as risk to distribution infrastructure from such things as landslide, washout and earthquake. These are not new risks; the company experienced several washouts due to wetter than normal conditions in 1999 that jeopardized the integrity of some portions of the company's distribution system. The Stipulation provides for a 5-year treatment of the cost to NW Natural of assessing geohazard risk, minimizing risk where possible, and repairing damage to facilities caused by geohazards. Staff and other parties were particularly concerned that the company could incur costs and request cost recovery for costs not associated with geohazard risk. The Stipulation specifies the types of risk that are covered, and the rate treatment that may be used depending on the nature of the work performed to repair geohazards. Specifically, under the Stipulation the company would not request cost recovery for what are typical O & M costs (that are already included in base rates) incurred to maintain and repair its distribution system, and would request cost recovery for assessing, mitigating or repairing geohazard risks.

NW Natural Advice No. OPUC 01-20 Bare Steel Replacement Program  
September 19, 2001  
Page 3

#### Rate Spread and Rate Design

NW Natural engineers estimated that the company's distribution and transmission facilities in Oregon included about 100 miles of uncoated steel plant. About 70 percent of the facilities are mains and services that serve principally residential and commercial customers. The remaining 30 percent consists of medium- and high-pressure facilities that serve all customers on the company's system. Using this engineering analysis, Staff and the other parties agreed that the company will allocate 70% of the cumulative investment to residential and commercial customers, spread on an equal cents per therm basis to those customers, and will allocate the remaining 30% of the cumulative investment to all customers, spreading this amount on an equal percent of margin basis. The initial rate changes that will occur as a result of the safety programs will be on or after October 1, 2002. The Stipulation is silent on the rate spread for the Geohazard Risk Mitigation and Repair Program. Rate spread will be addressed when NW Natural files for rate recovery of those costs.

#### The Stipulation

On August 3, 2001, NW Natural and Staff entered into a Stipulation which will allow the company to replace its bare steel distribution and transmission facilities within twenty years, and monitor and minimize "geohazards" such as landslide and washout that may damage distribution and transmission facilities and thereby cause service disruption or present safety problems. The Stipulation provides for recovery of program costs; Schedule 177 implements cost recovery for the bare steel portion of the Stipulation. The Stipulation contains provisions for Staff audit of the company's safety programs and annual reporting of progress on each of the programs. A copy of the Stipulation is attached as Exhibit A.

#### Proposed Safety Program Costs

The company included with its filing a worksheet showing an estimate of the cost of service for the bare steel replacement program. Assuming the entire \$3,000,000 in incremental bare steel replacement investment is made in a given year, the approximate cost of service associated with this investment is \$505,000. Under the terms of the Stipulation, residential customers on Schedule 2 would have a rate increase of .104 cents per therm. Commercial customers on Schedule 3 would have a rate increase of .098 cents per therm, while industrial customers on Schedule 91 (transportation customers) would see a rate increase of .003 cents per therm.

#### Deferred Accounting Application

Pursuant to ORS 757.259(2)(e), the company has requested deferred accounting treatment as necessary or required to record in appropriate sub-accounts of Account 186 any expenses eligible for rate treatment under the terms of the Stipulation for later treatment in rates in accordance with this filing. Deferred accounting is warranted in order

NW Natural Advice No. OPUC 01-20 Bare Steel Replacement Program  
September 19, 2001  
Page 4

to "match appropriately the costs borne by and benefits received by ratepayers." NW Natural estimates that through September 30, 2021, the company will spend approximately \$3 million per year in program costs for accelerated bare steel replacement and an undetermined amount for geohazard risk mitigation and repair. Deferrals will begin October 1, 2001. NW Natural's request is consistent with the requirements of ORS 757.259, OAR 860-027-0300, and the terms of the Stipulation. Staff recommends approval.

**STAFF RECOMMENDATIONS:**

I recommend the Commission take the following action regarding the NW Natural filing:

1. Allow the tariff sheets filed in Advice No. 01-20 to go into effect on October 1, 2001 (there are no rate changes in the tariff at this time).
2. Approve the rate spread used to spread the costs of the Bare Steel Replacement Program.
3. Approve the company's deferred accounting application for its safety program costs.
4. Approve the Stipulation, dated August 3, 2001, between NW Natural and Staff regarding rate treatment for NW Natural Safety Programs.

NW Natural Advice No. 01-20 Public Meeting Memo (Safety Programs)

Rates & Regulatory Affairs  
Integrated Resource Planning  
Facsimile: 503.721.2532



RECEIVED

August 3, 2001

AUG 10 2001

RATES &  
REGULATORY AFFAIRS

Bonnie Tatom, Manager  
Natural Gas Rates & Planning  
Public Utility Commission of Oregon  
550 Capitol Street, Northeast, Suite 215  
Salem, Oregon 97301-2551



Re: Safety Program Stipulation

Enclosed are two originals of the company's Safety Program Stipulation. Please sign both where indicated and return one original. A self-addressed, stamped envelope is enclosed for your convenience.

Please call me at 1-503-721-2452 if you have any questions or require any further information.

Sincerely,

Susan K. Ackerman, Manager  
Regulatory Affairs & Associate Counsel

SKA/cmt  
enclosures

**SAFETY PROGRAM STIPULATION**

**Date Entered:** August 3, 2001  
**Parties to Stipulation:** Northwest Natural Gas Company ("NW Natural" or "Company"); Oregon Public Utility Commission Staff ("Staff")

**Regarding:** Rate Treatment for NW Natural Safety Programs

1. This Safety Program Stipulation ("Stipulation") between NW Natural and Staff sets forth the terms the parties will support for rate treatment of NW Natural's natural gas transmission and distribution safety program(s). These programs ("safety programs") consist of (a) a long-term accelerated bare steel replacement program; and (b) a geohazard risk mitigation and repair program.
2. The parties agree that the safe and reliable operation of NW Natural's natural gas transmission and distribution system is necessary to providing adequate service to natural gas customers. The parties agree that the safety programs described in this Stipulation are intended to assist in maintaining a safe and reliable natural gas transmission and distribution system in NW Natural's Oregon service area.
3. NW Natural agrees to file, and Staff agrees to support, a tariff implementing the agreements set forth below in this Stipulation.
4. **Accelerated Bare Steel Replacement Program.** The parties agree that NW Natural's current natural gas transmission and distribution network in Oregon contains approximately 100 miles of bare (uncoated) steel plant. Bare steel plant consists of medium pressure mains and services, high pressure feeders, and ultra high pressure transmission, was installed in the 1940s, 1950s and early 1960s, and has been fully depreciated on the Company's books. The parties agree that replacing and retiring the bare steel portion of the Company's system will assist in maintaining a safe and reliable natural gas transmission and distribution system. The parties further agree that NW Natural is currently investing in a combined leakage and bare steel replacement program at a rate of investment of approximately \$3 million annually. At this level of investment, NW Natural estimates that bare steel plant will be replaced in approximately 37 to 40 years. Staff and the Company agree that an additional investment averaging approximately \$3 million annually will assist the company in a reasonably-expedited replacement of the bare steel plant. Staff and the Company agree that the rate treatment described in the following

paragraphs is just and reasonable because it supports accelerated replacement of the bare steel in the Company's transmission and distribution system.

- 4.0 NW Natural agrees to undertake a capital investment program to replace the Company's bare steel plant in its entirety by December 31, 2021. Toward this end, the Company agrees to annually budget capital towards an accelerated bare steel replacement program in an amount averaging approximately \$3 million beginning in 2001 and in years following as required to replace the bare steel plant by the end of 2021.
- 4.1 The parties agree that the accelerated capital investment for bare steel replacement should average about \$3 million annually. The parties agree that, in any given year, investment by the Company in its accelerated bare steel replacement program may total as much as \$6 million under the terms of this agreement. The parties agree that investment in accelerated bare steel replacement exceeding \$6 million annually is not included in this program unless the parties agree otherwise. If in any year the Company's total investment in accelerated bare steel replacement is expected to exceed \$6 million, then the Company will so advise Staff. Company and Staff agree to consult about appropriate rate treatment for that portion of the investment that may exceed \$6 million. For purposes of calculating accelerated bare steel replacement program costs subject to rate treatment under the terms of this Stipulation, the first \$3 million of leakage and bare steel replacement investment will be considered base investment. The amount of program costs in excess of the \$3 million base that is related to bare steel replacement will be considered accelerated bare steel replacement investment. Accelerated bare steel replacement program costs may include the costs of replacement of other types of distribution and transmission piping, such as coated steel or plastic piping, when replacement of other types is incidental to a bare steel replacement project.
- 4.2 The parties agree that, except as modified by paragraph 4.8 below, NW Natural may include in rates at the time of each annual Purchased Gas Adjustment (PGA) filing, or other suitable filing, revenue in an amount equal to the cost of service associated with the entire accelerated bare steel replacement program for the most recent 12 month period. The 12-month periods shall run from October 1 through September 30 of each calendar year, and may include supportable estimates of accelerated bare steel replacement investment for months where data is unavailable at the time of filing.



- 4.3 For each 12-month period, the company will develop a cost of service for the cumulative investment in the accelerated bare steel replacement program<sup>1</sup>. The cost of service will include incremental O&M expense, depreciation expense, property tax, return, income taxes and other costs customarily relating to a utility investment. The capital structure and the costs of long-term debt and preferred and preference stock to be used in the calculation of a return on rate base for the bare steel replacement program will be those adopted by the Commission in the Company's most recent general rate case. Exhibit A to this Stipulation depicts how the Company will develop a cost of service for each year's accelerated bare steel replacement program costs.
- 4.4 The Company's combined leakage and accelerated bare steel replacement program costs will be subject to an audit or other review by Staff at Staff's request. The audit is to be completed by June 30 of the year following the investment or such other time as is mutually agreeable. Staff's audit will provide the basis for any subsequent cost true-ups or adjustments. Cost true-ups or adjustments for each period will be included in program costs for the subsequent period, the net amount of which will be used in determining the cost of service for the subsequent year as described in paragraph 4.3 of this Stipulation.
- 4.5 At the time the Company files for rate treatment of its safety program in accordance with paragraphs 4.2 and 4.3 of this Stipulation, the Company will also submit a report to Staff containing sufficient information regarding the accelerated bare steel replacement program to assist in Staff review of the program. The report will contain information regarding the Company's activity for the 12 months for which rate treatment is sought, as well as on progress towards complete replacement of bare steel in accordance with paragraph 4.0 of this Stipulation. Exhibit B to this Stipulation is a list of the information the company will provide Staff.
- 4.6 To the extent the Company can quantify expense savings associated with the accelerated bare steel replacement program, the Company agrees to identify and report the benefits and to reflect a mutually agreeable adjustment to the amount of rate recovery in the subsequent year's filing.

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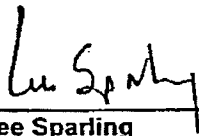
<sup>1</sup> Cumulative investment means the cost of service calculated each year for capital investment added in the most recent 12-month period plus the updated calculation of the cost of service for capital investment made in all prior periods.

- 4.7 Rate treatment of the accelerated bare steel replacement program as provided in this Stipulation will begin with the effective date of the Company's 2001 PGA filing, currently scheduled to be effective October 1, 2001, and every succeeding year until the bare steel facilities are replaced in their entirety in 2021.
- 4.8 If at any time between the effective date of this Stipulation and completion of the accelerated bare steel replacement program the Company files a request for a general rate review, then such request will include an appropriate adjustment to prohibit a double recovery of test period program costs. To the extent that accumulated prior period program investments are included in base rates in the general rate case, the stipulated rate treatment in subsequent years will reflect annual changes in cost of service for these prior period investments.
- 4.9 NW Natural agrees to file a tariff to collect the cost of service of the cumulative investment in the accelerated bare steel replacement program described in this Stipulation. The tariff will spread the cost of service of the cumulative investment as provided in this paragraph 4.9. The company will allocate 70% of the cumulative investment to residential and commercial customers, and will spread this amount on an equal cents per therm basis to residential and commercial customers. The company will allocate the remaining 30% of the cumulative investment to all customers, residential, commercial and industrial customers, and will spread this amount to all customers on an equal percent of margin basis.
5. **Geohazard Risk Mitigation and Repair.** The parties agree that recent wetter-than-average and other geologic conditions in NW Natural's service area pose risk to the public and to the safety and reliability of the company's distribution and transmission system from landslide, washout, earthquake and other geologic events (collectively, "geohazards"). The parties agree that assessing geohazard risk, monitoring geohazard risk sites, preventing damage from geohazards and repairing or replacing plant actually damaged by geohazards are all necessary to a safe and reliable transmission and distribution system. The parties agree that the rate treatment for costs associated with geohazard repair and risk mitigation, all as described in this paragraph 5 of this Stipulation, is just and reasonable.
- 5.0 NW Natural agrees to maintain a program of geohazard risk assessment, and to undertake reasonably necessary and prudent geohazard repair or risk mitigation as required to maintain a safe and reliable distribution and transmission system.

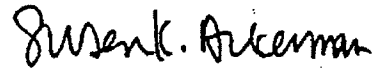
- 5.1 The parties agree that NW Natural may include in rates the costs associated with geohazard mitigation and repair as described in this paragraph 5 of this Stipulation to the extent that these costs are incremental to costs already embedded in permanent rates and to the extent that these costs are reasonably incurred.
- 5.2 If geohazard repair or risk mitigation imposes costs on the Company of the type customarily treated as capital investment in utility plant, then NW Natural may recover the cost of service of that investment in rates at the time of the next most recent PGA filing, or other suitable filing, following the investment. A cost of service for these capital expenses will be developed, and return will be determined, in accordance with the procedure outlined in paragraph 4.3 of this Stipulation.
- 5.3 If geohazard repair or risk mitigation imposes incremental O&M costs on the Company of the type customarily treated as utility expense, then NW Natural may defer such expense in a subaccount of Account 186 for later amortization in rates. Amortizations of such expenses will begin at the time of the next PGA filing. The Company agrees to annually file an application for deferred accounting (pursuant to O.R.S. 757.259) treatment, concurrently with each PGA filing, covering prospective expense associated with geohazard repair and risk mitigation.
- 5.4 The amounts to be included in rates due to the geohazard risk mitigation and repair will be subject to an audit or other review by Staff. Such review will be completed by June 30 of the year following the investment or repair.
- 5.5 These paragraphs 5 through 5.5 of this Stipulation governing geohazard repair and risk mitigation will terminate on December 31, 2006 such that geohazard repair and risk mitigation activity occurring after December 31, 2006 will not receive the rate treatment described herein unless further agreed between Staff and Company. Geohazard repair and risk mitigation activity occurring in the year prior to termination of this program on December 31, 2006 will be treated in accordance with Paragraphs 5.2, 5.3, and 5.4 of this Stipulation in the Company's 2007 PGA or similar filing. If the Company files for a general rate increase prior to December 31, 2006, then either Staff or Company may propose, in the rate case, an alternative treatment of geohazard risk mitigation and repair costs for prospective application following the conclusion of the rate case.

6. The parties' continuing agreement to this Stipulation is conditioned on Commission approval of the terms set forth herein. If at any time the Commission approves terms and conditions governing a bare steel replacement program or a geohazard risk mitigation and repair program that are different from the terms and conditions set forth in this Stipulation, then the parties will discuss whether the terms are acceptable and may negotiate changes acceptable to the Commission and parties. If either party cannot accept the Commission's changes and alternative terms cannot be agreed upon, then either party may terminate this Stipulation or any thereof by giving written notice to the other.
7. Either party may propose prospective changes to the terms in this Stipulation. Company and Staff agree to negotiate in good faith regarding any proposed changes. Any prospective changes to the terms of this Stipulation that the parties may agree upon shall not affect the rights and obligations that have already accrued under this Stipulation prior to any agreed upon change.

So Stipulated:



Lee Sparing  
Administrator,  
Electric & Natural Gas Division  
Oregon Public Utility Commission



Susan Ackerman  
Manager, Regulatory Affairs  
and Associate Counsel  
NW Natural

ORDER NO. 01-843

NWN Advice No. OPUC 01-20/Exhibit A  
Page 8 of 11

BEFORE THE OREGON PUBLIC UTILITY COMMISSION



Attachment A

BARE STEEL PROGRAM  
DETERMINATION OF COST OF SERVICE

TO

COMPANY'S SAFETY PROGRAM STIPULATION

OF

AUGUST 3, 2001

NW Natural  
Bare Steel Program  
Determination of Cost of Service (\$000)

	<u>Amount</u>
1 Rate Base - net of 1/2 year deprec. & def. tax	\$2,952
2 Operations and Maintenance	0
3 Depreciation	86
4 Property Taxes	42
<b>Taxes on Equity Return</b>	
5 State	17
6 Federal	83
7 Total Taxes	<u>100</u>
<b>Return on Rate Base</b>	
8 Debt	109
9 Preferred Equity	10
10 Common Equity	144
11 Total Return	<u>263</u>
12 Subtotal Cost of Service	491
13 Revenue Sensitive Items	<u>14</u>
14 Total Cost of Service	<u>\$505</u>

Cost of Capital			Weighted
	% of Capital	Cost	Cost
Debt	47.51%	7.75%	3.68%
Preferred Equity	4.78%	7.06%	0.34%
Common Equity	47.71%	10.25%	4.89%
	<u>100.00%</u>		<u>8.91%</u>
State Tax Rate			6.60%
Federal Tax Rate			35.00%
Revenue Sensitive Rate			2.813%
Depreciation Rate			2.87%
Property Tax Rate			1.39%
Incremental Investment			<u>\$3,000</u>

Income Taxes	
Gross up of Equity Return	254
Less: State tax	17
Federal Taxable income	<u>237</u>
Less: Federal Tax	83
Return	<u>154</u>

<b>Deferred Taxes</b>	
Book Depreciation	86
Tax Depreciation	113
Book-Tax Difference	26
Tax Effect	10
Deferred Taxes - 1/2 year convention	5

ORDER NO. 01-843

BEFORE THE OREGON PUBLIC UTILITY COMMISSION



**NW Natural**

Attachment B

ACCELERATED BARE STEEL REPLACEMENT AND  
LANDSLIDE PROGRAMS ANNUAL REPORT FORM

TO

COMPANY'S SAFETY PROGRAM STIPULATION

OF

AUGUST 3, 2001

**Attachment B**

The following describes the minimum information to be included in the Company's Annual Report to OPUC Staff regarding the Accelerated Bare Steel Replacement and Landslide Programs. Annual activity will be reported in terms of totals as of September 30. Amounts for the current year as included will be in the form of unaudited results as recorded. Additional descriptive information included as deemed necessary.

Summary for the period ending: \_\_\_\_\_

Description	Current Filing Year	Current 12 months	Program To Date
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Bare Steel Expenditures (\$000) [1]:

Total Leakage Capital [2]:

Total Bare Steel Program

Total Leakage Repair (O&M):

Annual Activity – counts :

Total Oregon system "B" Leaks

Total Oregon "B" leaks – Bare Steel

Total Oregon system "C" Leaks

Total Oregon "C" leaks – Bare Steel

Bare Steel Program Summary

Bare Steel Replaced (in miles):

Medium Pressure Mains & Svcs

High Pressure Feeders

Ultra High Pressure Transmission

LandSlide Program Expenditures [1]:

Total Capital Cost

Current Large Projects Highlights  
(as deemed appropriate)

[1] Those costs reflected in the most recent Rate Filing

[2] Total leakage costs includes base amount in rates



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**BEFORE THE PUBLIC UTILITY COMMISSION  
OF OREGON**

UM \_\_\_\_\_

In the Matter of  
NORTHWEST NATURAL'S System  
Integrity Program

**PARTIES' BRIEF IN SUPPORT  
OF STIPULATION**

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**I. INTRODUCTION**

Pursuant to OAR 860-014-0085(1) and OAR 8860-014-0085(4) NW Natural, along with Citizens Utility Board of Oregon ("CUB"), Public Utility Commission of Oregon ("Commission") Staff ("Staff") and the Northwest Industrial Gas Users ("NWIGU") (together, the "Parties") file this brief in support of their stipulation regarding the Company's new System Integrity Program ("SIP") which is described in Draft Revised Schedule 177, entered into on October 16, 2008 ("the Stipulation"). In the Stipulation, the Parties agree that (a) the Commission should approve the SIP's proposed integration of the Company's current and proposed safety initiatives; (b) the Company's costs associated with the SIP program should be treated as capital expenditures; and (3) the SIP costs should be recovered in the same manner as the Company is currently recovering costs associated with its existing safety programs--Transmission Integrity Management Program ("TIMP") and its Bare Steel Replacement Program ("Bare Steel").

As will be described in more detail below, the SIP program will benefit customers by integrating new and existing safety programs, thus, allowing for more efficient and effective identification of risks, and ensuring that the Company targets safety program funds where the need is most pressing. In addition, the costs of implementing the SIP will be capital in nature and should be so characterized. Third, the cost recovery framework proposed by the

1 Parties is a reasonable one. For these reasons the Commission should approve the  
2 Stipulation and allow Advice No. 08-XXX to go into effect.

3 **II. BACKGROUND**

4 **A. NW Natural's Current Safety Programs Tariff**

5 NW Natural is proposing revisions to its Schedule 177, Adjustments to Rates for  
6 Safety Programs. As it currently exists, Schedule 177 describes the adjustments to rates  
7 for costs associated with three separate safety-related programs: the Bare Steel Program,  
8 the Geohazard Repair and Risk Mitigation Program ("Geohazard Program") and TIMP.<sup>1</sup>  
9 Pursuant to Commission orders and practice, the costs associated with all of these  
10 programs are recorded as capital expenditures. The Company's proposes to revise  
11 Schedule 177 to reference one integrated safety program – the SIP – which combines the  
12 existing Bare Steel and TIMP programs with a newly developed Distribution Integrity  
13 Management Program ("DIMP"). The Draft Revised Schedule 177 is attached as Exhibit A  
14 to the Stipulation, filed contemporaneously with this brief.

15 **B. NW Natural's Bare Steel Replacement Program**

16 In 2001, the Company initiated its current Bare Steel Replacement Program, which  
17 allows for the accelerated replacement of the Company's bare steel distribution and  
18 transmission facilities.<sup>2</sup> The purpose of the program is to replace transmission facilities and  
19 distribution mains and services constructed from aging bare steel, which is prone to  
20 corrosion and leakage, with pipes made from corrosion-resistant "polyethylene pipe or  
21 coated, cathodically protected steel pipe." This project is scheduled to conclude in 2021.<sup>3</sup>

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24 <sup>1</sup> This program has previously been referred to as the Integrity Management Program. The  
25 Company has renamed the program in order to distinguish it from the DIMP, discussed below.

26 <sup>2</sup> See Advice No. 01-20.

<sup>3</sup> Order No. 01-843

1 **C. NW Natural's Transmission Integrity Management Program**

2 In 2002, Congress passed the Pipeline Safety Improvement Act ("2002  
3 Improvement Act") and, in accordance with its terms, the Office of Pipeline Safety and the  
4 Research and Special Programs Administration issued a new rule that added incremental  
5 requirements on the operators of transmission pipelines —Pipeline Integrity Management in  
6 High Consequence Areas (Gas Transmission Pipelines) (the "IMP Rule").<sup>4</sup> The IMP Rule  
7 requires operators to identify transmission lines in certain "high consequence areas" and to  
8 implement written integrity management programs for such areas.

9 To carry out the work required under the IMP Rule, NW Natural developed its TIMP.  
10 In UM 1156, the Company filed an application requesting an accounting order classifying  
11 the TIMP costs as capital expenditures. In support of its application, the Company pointed  
12 out that the work required under the 2002 Improvement Act would ultimately result in an  
13 extension of the useful life of NW Natural's transmission lines,<sup>5</sup> and further, was required to  
14 continue operation of covered sections of NW Natural's transmission pipeline without  
15 pressure reductions.<sup>6</sup> The Company also explained that the work required under the IMP  
16 Rule was incremental to pre-existing safety regulations and therefore was incremental to  
17 and not duplicative of pre-existing safety costs.<sup>7</sup> Staff supported the Company's  
18 application,<sup>8</sup> and in Order 04-390 the Commission approved NW Natural's request.<sup>9</sup>

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21 <sup>4</sup> 69 Fed. Reg. 2307 and corrected in 69 Fed. Reg. 18277.

22 <sup>5</sup> Application, p. 5.

23 <sup>6</sup> *Id.*

24 <sup>7</sup> *Id.* p. 6.

25 <sup>8</sup> See Staff Memorandum.

26 <sup>9</sup> At the same time, the Commission approved NW Natural's request for recovery of costs associated with the program through the company's annual Purchased Gas Adjustment (PGA) filing. The rate recovery treatment approved by the Commission in Order 04-390 was proposed to expire as of September 30, 2008.

1 **D. NW Natural's Distribution Integrity Management Program**

2 In 2006 Congress passed the Pipeline Inspection, Protection, Enforcement and  
3 Safety Act ("2006 PIPES Act") which expands the scope of the 2002 Improvement Act, by  
4 requiring the Department of Transmission Pipeline and Hazardous Material Safety  
5 Administration ("PHMSA") to prescribe minimum standards for Distribution Integrity  
6 Management Programs ("DIMPs") for distribution mains, services and other gas related  
7 appurtenances. In addition, the PIPES Act significantly increases the requirements of all  
8 stakeholders relative to excavation damage prevention. Based on the Congressional  
9 mandate, PHMSA issued a Notice of Proposed Rulemaking (NPR) for "Pipeline Safety:  
10 Integrity Management for Gas Distribution Pipelines" on June 25, 2008.<sup>10</sup> The DIMP NPR  
11 is substantially based on the "Integrity Management for Gas Distribution, Report of Phase 1  
12 Investigations" completed in December, 2005, and prescribes a high level, flexible  
13 regulation that will require each operator of natural gas distribution systems to implement a  
14 DIMP that includes seven defined elements, including:

- 15 1) Knowledge of the characteristics of the system
- 16 2) Identify threats
- 17 3) Evaluate and prioritize risk
- 18 4) Identify and implement measures to address risk
- 19 5) Measure performance and evaluate effectiveness of the Program
- 20 6) Periodic evaluation and improvement
- 21 7) Report results of performance metrics to regulators<sup>11</sup>

22 In order to comply with these proposed regulations, operators will gather and  
23 integrate data from a wide range of sources, including: incident and leak history; corrosion  
24 control records; continuing surveillance records; patrolling records; maintenance history

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25 <sup>10</sup> 49 CFR Part 192, Docket No. PHMSA – RSPA-2004-19854.

26 <sup>11</sup> 73 Fed. Reg. 36015, 36021 (June 25, 2008).

1 and "one call" and excavation damage experience.<sup>12</sup> The data from these sources must be  
2 mined and integrated into a single database that allows operators to conduct a relative risk  
3 analysis to identify facilities or groups of facilities that are subject to higher risk. The data  
4 mining and integration may involve extensive efforts and / or new computer software or  
5 programming. After completion of the relative risk ranking, operators will be required to  
6 implement additional or accelerated measures to address risks.<sup>13</sup> At a minimum, operators  
7 will be required to implement two risk reduction strategies: an effective leak management  
8 program and an enhanced damage prevention program.<sup>14</sup> The Gas Piping Technology  
9 Committee developed guidance in parallel with the DIMP NOPR to provide operators with  
10 additional examples of compliance with the proposed rule.<sup>15</sup>

11 NW Natural is currently developing a DIMP program for the Company so that it will  
12 be prepared to comply with the final Rule, once it is adopted.

13 **E. NW Natural's Geohazard Program**

14 NW Natural's Geohazard Program, which was developed to assist the Company in  
15 identifying geological conditions posing threats to the Company's distribution and  
16 transmission pipelines, expired on December 31, 2006, except for one specific project that  
17 was approved for completion prior to December 31, 2007.<sup>16</sup> However, the Company's  
18 activities under that program are mandated under the TIMP, and the proposed DIMP, both  
19 of which require the Company to assess all threats to pipelines and related facilities  
20 including threats posed by "outside forces," including geological threats.<sup>17</sup> For these

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21 <sup>12</sup> *Id.* at 36033

22 <sup>13</sup> *Id.*

23 <sup>14</sup> *Id.*

24 <sup>15</sup> *Id.* at 36024

25 <sup>16</sup> Order No. 07-444.

26 <sup>17</sup> Threat identification is addressed in the IMP Rule, 49 CFR, Part 192, Subpart O Section 192.917(a) which states: "An operator must identify and evaluate all potential threats to each covered pipeline segment. Potential threats that an operator must consider are listed in ASME

1 reasons, the activities formerly undertaken by the Company under the Geohazard Program  
2 will be incorporated into the TIMP and DIMP and the Company will therefore not request  
3 that the Commission renew the Geohazard Program.

4 **F. NW Natural's New System Integrity Program**

5 In an effort to increase efficiency, the Company is now proposing that all actions  
6 taken pursuant to the TIMP, DIMP and Bare Steel Programs<sup>18</sup> be combined into one  
7 integrated System Integrity Program ("SIP"). Through this integration, the Company will  
8 coordinate all system integrity efforts, and prioritize activities to address the greatest risks  
9 to the Company's system, regardless as to which of the specific program parts are  
10 implicated. Creation of a new, integrated program will allow NW Natural to minimize  
11 administrative costs and avoid any duplication of effort. Most importantly, integration of  
12 these safety programs will result in a safer system for the Company's customers and the  
13 public at large.

14 **III. THE STIPULATION**

15 **A. Accounting Treatment**

16 In Paragraph 6 of the Stipulation, the Parties have agreed to support NW Natural's  
17 Petition for Accounting Order to classify SIP costs as capital costs. The Parties agree that  
18 the costs associated with the three component programs that will be under the SIP  
19 "umbrella"—the Bare Steel Program, the TIMP and the DIMP—are all properly  
20 characterized as capital expenditures, and therefore the SIP costs in general should be  
21 recorded as capital.

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25 B31.8S, which includes "weather related and outside force, earth movements.: In addition, the  
26 NOPR for the proposed DIMP rule requires operators to consider outside forces that could threaten  
the integrity of the pipeline.

26

1           The Oregon Attorney General's office has defined "capital expenditure" as "an  
2 expenditure for long-term additions or betterments properly chargeable to a capital asset."<sup>19</sup>  
3 The Bare Steel Program Costs clearly fall under this definition and have always been  
4 treated as capital costs. Moreover, the Commission has already agreed that the costs  
5 associated with NW Natural's TIMP Program should be recorded as capital expenditures.<sup>20</sup>  
6 Like the TIMP costs, the DIMP costs will be incurred as a result of complying with Federal  
7 regulations, and are therefore necessary to the Company's continued operations. Similarly,  
8 as with the TIMP, all actions taken in furtherance of the DIMP will serve to extend the  
9 useful life of pipelines (in this case, distribution instead of transmission) and related  
10 facilities. For these reasons the Parties agree that the Commission should grant NW  
11 Natural's Petition and issue a ruling allowing the Company to record SIP expenses as  
12 capital expenditures.

13 **B. Cost Tracking**

14           The Stipulation lays out a method of cost tracking that will ensure that all SIP costs:  
15 (a) are accounted for; and (b) will include only those costs incurred by the Company that  
16 are incremental to costs otherwise recovered by the Company.

17           Paragraph 7 provides that the Company will track SIP costs on a project basis.  
18 Project costs would accumulate in specific SIP-designated capital accounts and would be  
19 tracked on a per-job basis. The Company would track the SIP investment annually to  
20 obtain a total account for each year, with the proposed tracking period running from  
21 November 1 to October 31 (the "Tracker Year").<sup>21</sup> In order to ensure that customers are  
22 protected, pursuant to paragraph 8 of the Stipulation, the Company will track costs

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24 <sup>19</sup> Letter from Donald C. Arnold, Chief Counsel, General Counsel Division, Oregon Dept. of Justice,  
25 to Catherine E. Pollino, Director, Audits Division, Oregon Secretary of State, 3-4 (May 28, 2002).

26 <sup>20</sup> See Order No. 04-390

<sup>21</sup> For the 2008-2009 year, the relevant period would be October 1, 2008 to October 31 2009.

1 specifically to ensure that SIP costs do not include any costs associated with the SIP  
2 programs that are currently being recovered as O&M costs.

3         The SIP costs will be tracked from November 1 prior to the PGA filing date, plus an  
4 estimate of activity through October 31, in order to determine the SIP Cost of Service—as  
5 described below. All costs will be subject to audit by PUC Staff. The SIP Cost of Service  
6 would be included in the Company's PGA filing. Upon Commission approval of the SIP  
7 Cost of Service, an adjustment would be made to permanent rates in Schedules 1-3, 31,  
8 32, 33 and 54.

9 **C. Cost Recovery**

10         1. SIP Cost of Service

11         The SIP Cost of Service would be identified using the same process that was  
12 approved by the Commission in UM 1156 to calculate the TIMP costs, and in UM 1030 to  
13 calculate the Bare Steel and Geohazard Program costs.<sup>22</sup> That is, for each Tracker Year,  
14 the Company would develop a cost of service based on the revenue requirement for the  
15 SIP investment costs which would include incremental depreciation, expense, property tax,  
16 return on investment, income taxes and other costs customarily relating to utility  
17 investment. The capital structure and cost of long term debt and preferred stock to be used  
18 in the calculation of a return on rate base would be those adopted by the Commission in  
19 NW Natural's most recent rate case.

20         The Parties agree that, subject to audit, the rates would be adjusted each fall within  
21 NW Natural's PGA, in the same manner used for recovery of costs for the TIMP, again as  
22 prescribed in Order 04-390.

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26 <sup>22</sup> See Order Nos. 04-390, 02-687, 01-843 and Schedule 177.



1           2. Costs Not To Be Recovered

2           In paragraph 8 of the Stipulation the Parties have agreed that the Company will not  
3 seek recovery through the Stipulation's recovery mechanism for the approximately \$574  
4 thousand per year in O&M costs that are currently embedded in rates. In addition, as a  
5 benefit to customers, the Parties have agreed the Company will not seek recovery through  
6 the proposed annual rate adjustment for: 1) additional O&M costs related to DIMP damage  
7 prevention, 2) the first \$3 million in combined bare steel and leakage capital costs, and 3)  
8 an additional \$250,000 in SIP capital costs. See attached Exhibit B.

9           3. Recovery Cap

10          In paragraph 10 the Parties have agreed that total annual SIP costs recoverable  
11 would be subject to a soft cap of \$12 million with \$8.176 million recoverable as SIP Cost of  
12 Service—except for 2008 where current program approvals for Bare Steel and TIMP are  
13 applicable. Recovery of SIP costs in excess of the limits in this paragraph would be only  
14 with the written consent of the Parties.

15 **D. Cost Allocation**

16          The Parties agree that costs will be recovered through one adjustment schedule—  
17 Schedule 177, which will be comprised of three Parts.

18          Part A will account for costs related to the Bare Steel Program, for which 70% of  
19 costs will continue to be allocated to Residential and Commercial firm sales and  
20 transportation and customers taking service under Rate Schedules 1, 2, 3, 31, and 54. The  
21 remaining 30% will be spread to all customer classes on an equal percent of margin basis.

22          Parts B and C will account for TIMP and DIMP costs respectively, both of which will  
23 be spread to all customer classes on an equal percent of margin basis.

24          The Parties agree that these allocation methods best reflect the benefits to be  
25 realized to the respective customer classes.

26

1 **E. Annual Forecast and Report**

2 In order to help the Parties assess the future impact of SIP recovery, each April, all  
3 Parties will receive a forecast of expenses through October 31 2011, broken down into  
4 Parts A, B and C as described above. However, the Company will have the flexibility to  
5 shift dollars between the three Parts based on NW Natural's assessment of annual risk and  
6 need. Each August, the Parties will receive a report of actual SIP expenses by Tracker  
7 Year, broken down by specific projects and initiatives.

8 **F. Bare Steel Program**

9 In 2001, the OPUC Staff and NW Natural entered into a stipulation regarding the  
10 Bare Steel Program to allow the Company to replace its bare steel distribution and  
11 transmission facilities within twenty years.<sup>23</sup> The intent of this Stipulation is to allow funds  
12 previously earmarked for bare steel to be shifted among all three of the SIP component  
13 programs.

14 NW Natural will maintain its obligation under the Bare Steel Stipulation to complete  
15 the replacement of its bare steel distribution and transmission facilities by 2021. Upon  
16 expiration of the SIP Stipulation, the Parties agree that the Bare  
17 Steel Stipulation will remain in effect.

18 **G. Term**

19 In paragraph 16, the Parties agree that the Stipulation will apply to costs incurred  
20 *after* September 30, 2008 and *up to* the earlier of October 31, 2011, or the effective date of  
21 new rates implemented from Company's next general rate case.

22 **H. Commission May Request Rate Case**

23 In order to provide additional protection for customers the Parties agree in  
24 paragraph 15 that, at any time after July 1, 2009 the Commission may request that the  
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26 <sup>23</sup> See Order No. 01-843.

1 Company file a rate case, and that the Company must submit a general rate filing within  
2 eight months thereafter. In addition, NW Natural will bear the burden of proof in such filing.

3 The Parties recognize that in UG 163/UG 152, the parties to the stipulation adopted  
4 in that docket agreed that, subject to certain conditions and exceptions, the Company  
5 would not make a general rate filing before September 1, 2011. In recognition of the fact  
6 that these parties could reasonably view the terms of paragraph 15 as contradictory to the  
7 UG 163/UG 152 stipulation, NW Natural conferred with all parties to the UG 163/UG 152  
8 stipulation that are not parties to this Stipulation-- Northwest Energy Coalition, Oregon  
9 Department of Energy, and Community Action Development Organization. Each of these  
10 parties has confirmed that it has no objection to paragraph 15.

11 **IV. CONCLUSION**

12 For reasons set forth above, NW Natural respectfully requests that the Commission  
13 issue an order adopting the Stipulation, approving its request to classify all SIP expenses  
14 as capital, except for the O&M amount included in the Company's last general rate case

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1 and approving the Advice filing regarding the revisions to Schedule 177, approve the cost  
2 recovery mechanism described herein.

3

4 Dated: November 25, 2008

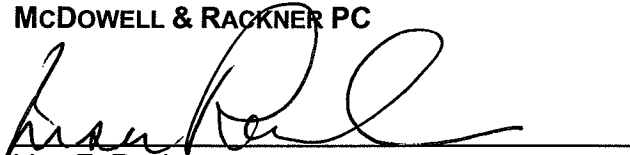
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Respectfully submitted,

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